Philipp M Hildebrand: The international monetary system

Opening remarks by Mr Philipp M Hildebrand, Chairman of the Governing Board of the Swiss National Bank, at the High-Level Conference on the International Monetary System, Zurich, 11 May 2010.

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I. Introduction

Good morning, Ladies and Gentlemen. It is a pleasure and special privilege to welcome you to this conference on the international monetary system. I am delighted that, together with the IMF, we have succeeded in bringing together such an outstanding group of policy makers and academics. I want to thank you for taking the time to join today's discussion at this critical juncture for the international monetary system.

I am especially grateful that the Managing Director of the IMF is with us today. Dominique, a very warm welcome to you. I know I speak on behalf of everyone here today when I say that we really appreciate your presence.

Conferences on the international monetary system are held with great regularity, particularly in the wake of financial crises. It is therefore not surprising that the recent crisis has brought renewed attention to the functioning of the international monetary system.

But as Herb Stein noted more than 40 years ago, it is not easy to define the international monetary system. Where does the international monetary system end and domestic economic policy begin? Did the recent crisis have its roots in shortcomings of domestic policies or in shortcomings of the international monetary system?

My role today as the opening speaker is a privileged one. Like a university professor during exams, I can ask questions. Unlike a good professor, I am certainly not in possession of all the answers. I am confident, however, that the exceptional group of people assembled here will make a positive contribution to this difficult and complex debate.

II. The problem

Arguably, much of the debate surrounding the international monetary system boils down to the following question: how sustainable is an international monetary regime, in which one national currency serves as the international reserve asset? Over the past few decades, this question has been examined under different perspectives.

A first perspective was the so-called "Triffin dilemma", discussed in the context of the Bretton Woods fixed exchange rate regime. This discussion highlighted that increasing indebtedness of the reserve-issuing country would in time undermine the very confidence that forms the basis for the reserve asset status.

A second perspective refers to the alleged "exorbitant privilege" of the reserve-issuing country. It highlights the asymmetry in the adjustment to shocks, as the reserve-issuing country has the privilege of not being under much pressure to adjust to current account deficits, at least over the short and medium term. It is worth noting that part of Keynes' goal in setting up the IMF was to try to create symmetry between the need to adjust for both deficit and surplus countries.

More recently, the question appeared under the perspective of global imbalances. This discussion highlights that current account surplus countries can forego, at least temporarily, the required adjustment by accumulating international reserves instead. The sustainability of these imbalances, and the extent to which they have contributed to the recent global financial crisis, is still under discussion.

The question of the reserve asset has often been at the center of the debate. But as Mark Carney has recently argued, the adjustment mechanism may be more important than the choice of reserve assets.

If adjustment were rapid, symmetric, and global, and if adjustment costs were fairly distributed amongst countries, we probably would not need to gather here today. Unfortunately, this is not the world we live in now.

Historically, exchange rate flexibility has often been the answer. While it is not a silver bullet, it remains true that adjustment through the exchange rate is usually faster, and in the end less costly than adjustment through prices and wages.

At the same time, of course, discontent with what is often perceived as excessive exchange rate volatility has been an important source of dissatisfaction with the present international monetary system. What constitutes excessive exchange rate volatility, and whether domestic policies or the international monetary system are at the root of it, is a matter of legitimate debate.

III. The conference

Nearly twenty years ago, Jacob Frenkel made the following observation about the international monetary system: “academics and policymakers have made numerous proposals for reform while, at the same time, the monetary system itself has been in a constant state of change”.

This points to another problem that any attempt to reform the international monetary system faces: the world economy and financial markets, and therefore the international monetary system never cease to evolve.

Today’s conference is organized around four panel discussions. They will focus on issues that are at the forefront of the current debate on shortcomings of the international monetary system. The first panel, chaired by Axel Weber, will discuss the predominant concerns about the present system.

Large global imbalances, volatile capital flows, and rapid reserve accumulation give rise to concerns about vulnerabilities. Are they possible sources of instability, and what reforms, if any, should be considered?

As I pointed out earlier, one recurring theme in the debate has been the question of reserve assets. Our second panel, chaired by George Soros, will examine ways to improve the supply of reserve assets.

Is a diversification of reserve assets desirable, and if so, should it be actively promoted? Is there a greater role for SDRs in the international monetary system, and if so, what reforms would be required to give SDRs a greater role?

Over the past decades, private capital flows have greatly increased. Although capital account liberalization is clearly beneficial in the long run, it entails significant short-run vulnerabilities.

The third panel, chaired by Duvvuri Subbarao, will take up the question of how to deal with these vulnerabilities. What are the appropriate policy responses, and what is the role for regulation and capital controls?

One policy response has been the accumulation of reserves, which can provide a temporary shock absorber. However, reserve accumulation entails costs for the countries accumulating reserves as well as for the world economy as a whole. Our last panel, chaired by Masaaki Shirakawa, will discuss alternatives to self-insurance. An obvious question here is the role of IMF lending facilities.

As already mentioned, the questions we address today are difficult and complex. Someone who played an important role in trying to address them over several decades was Jacques Polak. Sadly, he passed away earlier this year.

Reflecting on the efforts to reform the international monetary system since the Bretton Woods conference, Jacques Polak once suggested that "those of us who toil at the international monetary system would do well to adopt Sisyphus as our patron saint".

In honor of Jacques Polak, let us then push the stone back up the mountain once more and start with our first panel.

Thank you for your kind attention.